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THE WHITE HOUSE
WASHINGTON

CABINET AFFAIRS STAFFING MEMORANDUM

DATE: 3/8/82 NUMBER: 050174CA DUE BY: -------

SUBJECT: CABINET COUNCIL ON ECONOMIC AFFAIRS -- March 9 Meeting

	ACTION	FYI
ALL CABINET MEMBERS	☐	☐
Vice President	☑	☐
State	☑	☐
Treasury	☑	☐
Defense	☐	☑
Attorney General	☐	☑
Interior	☐	☑
Agriculture	☑	☐
Commerce	☑	☐
Labor	☑	☐
HHS	☐	☑
HUD	☐	☑
Transportation	☑	☐
Energy	☐	☑
Education	☐	☑
Counsellor	☑	☐
OMB	☑	☐
~~CIA~~	☐	☑
UN	☐	☑
USTR	☑	☐
CEA	☑	☐
CEQ	☐	☐
OSTP	☐	☐
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	ACTION	FYI
Baker	☑	☐
Deaver	☐	☐
Anderson	☑	☐
Clark	☑	☐
Darman *(For WH Staffing)*	☑	☐
Jenkins	☐	☑
Gray	☐	☑
Beal	☐	☑
Mike Wheeler	☑	☐
Larry Kudlow	☑	☐
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______	☐	☐
______	☐	☐
CCNRE/Boggs	☐	☐
CCHR/Carleson	☐	☐
CCCT/Kass	☐	☐
CCFA/McClaughry	☐	☐
CCEA/Porter	☑	☐

REMARKS:

Attached are the agenda and background papers for the Tuesday, March 9 (tomorrow's), meeting of the Cabinet Council on Economic Affairs, scheduled for 8:45 AM in the Roosevelt Room with PRINCIPALS ONLY.

Note that the paper for agenda item #2 will be distributed at the meeting.

RETURN TO: Craig L. Fuller
Assistant to the President
for Cabinet Affairs
456-2823

THE WHITE HOUSE

WASHINGTON

March 5, 1982

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: ROGER B. PORTER

SUBJECT: Agenda and Papers for the March 9 Meeting

The agenda and papers for the Tuesday, March 9 meeting of the Cabinet Council on Economic Affairs are attached. The meeting is scheduled for 8:45 a.m. in the Roosevelt Room.

The first agenda item is transportation user fees. Secretary Lewis has requested that the Council consider this issue. A paper, prepared by the Department of Transporation, entitled "Highway and Transit Systems: Meeting Unfunded Needs," is attached.

The second agenda item is a discussion of sectoral implications of defense expenditures. A paper on this issue, prepared by the Department of Commerce in coordination with the Department of Defense and the Council of Economic Advisers will be distributed to Council members at the meeting.

The third agenda item is a review of the near term future for the U.S. active shipbuilding base. A paper on this issue, prepared by the Department of Transportation, is attached.

Attendance at this meeting will be limited to principals only.

Attachments

THE WHITE HOUSE

WASHINGTON

CABINET COUNCIL ON ECONOMIC AFFAIRS

March 9, 1982

8:45 a.m.

Roosevelt Room

AGENDA

1. Transporation User Fees (CM#215)

2. Sectoral Implications of the Defense Buildup (CM#151)

3. Shipbuilding Assessment (CM#205)

HIGHWAY AND TRANSIT SYSTEMS: MEETING UNFUNDED NEEDS

A User Charge Proposal Consistent with New Federalism

THE ISSUE

The President's 1983 budget and legislative proposals provide adequate funding for transportation purposes, with two notable exceptions. The most visible and most heavily used parts of the system--our highway and public transit networks--are confronted with serious problems of physical deterioration far beyond the capacity of existing revenue sources. The existence of this funding shortfall has been clearly recognized by the states and threatens the success of the President's New Federalism initiative, as well as the Administration's user charge programs, particularly in transportation.

THE PROPOSAL

The proposal would increase annual highway user charges by the equivalent of 5 cents per gallon, beginning in FY 1983 (or January 1, 1984) to raise approximately $5 billion to bring current highway user charges into line with the level of expenditures required to maintain our highways and to help keep transit facilities in adequate condition. These revenues would be raised by a combination of a 4 cent gas tax increase and the equivalent of 1 cent from other highway user charges, such as heavy truck use taxes, so that all revenues are not directly raised from consumers. Approximately $4 billion of the increase would be used for highways and $1 billion per year would finance capital expenditures for mass transit (in lieu of building expensive urban freeways). The proposal provides essential maintenance of the transportation infrastructure to ensure economic growth and improved productivity. Finally, as discussed below, the proposal could have a significant positive impact over the next few years on the federal budget. This proposal is essential to the President's New Federalism commitment that programs turned back to the states are accompanied by adequate revenues.

HIGHWAY AND TRANSIT SYSTEM NEEDS

Numerous reports from system users, DOT data, national media attention and GAO investigations show that our highway and transit systems are seriously deteriorating. This situation has been developing for many years, and reflects several basic factors:

- Highway pavement conditions and congestion present serious problems to the efficient movement of goods and services.
  - More than 4,000 miles, a full 10% of the Interstate system, now needs immediate resurfacing or replacement.

- On some Interstate highways, traffic is limited to one lane, and on other highways, motorists must slow down to 30 mph due to potholes and ruined road surfaces.

- Almost half of the Interstate system will need major repairs by 1995, assuming present funding levels are maintained.

- More than 50% of Primary system pavement will reach the end of its design life during the 1980's, a 10-fold increase in deteriorated pavement since 1978.

o Bridges across the country are in truly grim shape.

- The useful design life of a bridge is 50 years, and 75% of our bridges are now over 45 years old.

- Two out of every five bridges are now judged deficient, and one out of five need immediate major rehabilitation.

- The total cost of needed bridge repairs now exceeds $40 billion and is increasing steadily each year.

o Mass transit systems are antiquated and service is declining.

- Older subway systems in our large cities are decaying and service is becoming unreliable, with some subway cars better suited for museums than continued service.

- It would require a one-time funding increase of $6 billion to replace transit buses over 15 years old and to reduce the average age of the Nation's fleet to 7.5 years.

- Unless transit facilities are maintained in safe, reliable operating condition, the economic viability of many large cities may be severely undermined.

o Transportation capital investments cannot be deferred as in some programs. The problems only get worse and the costs increase. For instance, a two or three year deferral of highway resurfacing work requires subsequent total reconstruction at triple the cost, plus inflation.

o The highway system is critical to the health of our economy -- 93 percent of all trips, 75 percent of all freight movements (by value), and 65 percent of all military shipments take place on the highway system.

o The purchasing power of highway user fees has been shrinking because of inflation over the last decade. The basic 4 cents per gallon highway user fee has not changed since 1959, while construction costs have gone up by 300%, making our original fees now worth less than a cent.

- o Existing financing sources fall far short of documented needs. All levels of government taken together are spending only half what is needed to keep highways serviceable.

A highway user charge increase of $5 billion per year is necessary to halt accelerating deterioration of our transportation infrastructure. These funds, along with continuing increases in state and local financing, will make it possible to reverse the trend towards deterioration and assure the continued efficiency of our transportation networks.

RELATIONSHIP OF THE PROPOSAL TO THE ADMINISTRATION'S PRINCIPLES OF USER CHARGES AND FEDERALISM

In two recent addresses to the Nation, President Reagan sounded themes which have particular relevance to the transportation funding programs in which the Federal Government is presently involved. First, in his September Address on the Program for Economic Recovery, the President stated his firm belief in user fees, particularly in transportation. He said, "When the Federal Government provides a service directly to a particular industry or to a group of citizens, I believe that those who receive benefits should bear the costs." Second, in his State of the Union Message, the President called for a "New Federalism" and outlined his plan for turning back 43 programs to the states, including several specific Federal transportation programs.

DOT enthusiastically supports New Federalism and believes there is no better area to achieve its objectives than in transportation.

The principles and objectives of New Federalism need not be reiterated here. But the user charge policy and the extent of our efforts to carry it out in the transportation sector deserve discussion. User charges, some of which include fuel taxes similar to those in highways, are the centerpiece of the Administration's plan to restore marketplace incentives for efficient transportation services, as well as to ensure that the costs are paid for by the users and beneficiaries of those programs. Table 1 summarizes the funding impacts of the current Administration proposals for transportation user charge cost recovery. Briefly, these proposals include:

- o Recovery of the costs of dredging deep draft harbors and their connecting channels by the Army Corps of Engineers. The Administration's proposals will shift the financial responsibilities to the states and localities and will allow them to recover the costs through user charges levied on the commercial interests that use the ports and channels.

- o Recovery of the costs of maintaining the inland waterways and their locks and dams. The Administration has made its intention clear to seek full cost recovery on the inland waterways in this session of Congress by increasing taxes from the fuel tax of six cents per gallon now being collected to a level equivalant to 32 to 38 cents per gallon (to be collected through a ton-mile fee).

- o Recovery of the costs of Coast Guard services which can be identified as benefiting special classes of users. Legislation to achieve that end has been prepared by DOT and is going through the clearance process.

- o Recovery of the costs of the Federally operated Air Traffic Control System. The Administration has proposed legislation to recover those operating, maintenance, and other costs in part through an escalating increase in aviation fuel taxes of up to 400% and passenger ticket tax increases of more than 60%.

User charges should not be considered as taxes imposed on the general taxpayer. Rather, user charges are paid by individuals according to the extent and character of their use of certain services. Furthermore, the question of whether to increase a user charge should not be constrained by fiscal policy, although programs fully financed by user charges may have positive effects on the budget balance. (See Table 2)

The user charges imposed in the Federal-aid Highway Program are the oldest and best model at the Federal level in transportation of the principle of users paying for services received. Funds flow from user fees directly into the Highway Trust Fund and from the Trust Fund to the states to finance highway and highway-related programs.

The highway program has also been one of the most successful and effective Federal programs, operating with a long tradition of shared Federal-state oversight. This assessment is reflected in the 1981 Heritage Foundation report on the Federal Government, which stated: "The Federal Highway Administration is generally regarded as an agency whose goals are clear and whose management has been generally effective."

The tradition of the present Federal-aid highway program is one in which states are accorded full authority for program decisions and implementation. Virtually all significant investment decisions in the highway program are made by state, not Federal, officials. The FHWA program is not among those programs created in the last 20 years which substituted for or usurped state authority. Instead it has provided support to states and localities for implementing their decisions.

In supporting urban mass transit, the Federal Government has, in recent years, provided both operating and capital assistance. This Administration has proposed legislation to phase out operating assistance but has strongly endorsed continued capital funding.

At the time of the President's announcement of the "New Federalism," the DOT was drafting legislation to put the remaining transit capital assistance programs on a "block grant" basis in order to afford maximum flexibility to states and local governments. The proposal to turn those programs over to the states is a logical extension of DOT's plans and makes good sense.

It is consistent with the user charge philosophy to use one cent from highway related charges for mass transit. If transit is allowed to deteriorate, it will be necessary to provide compensating additional highway capacity. The cost of urban freeway, parking, and even housing facilities would be much greater than the expenditures needed to preserve the mass transit infrastructure. For instance, urban freeway projects such as Westway in New York and Century Freeway in Los Angeles can cost up to $300 million per mile. Further, the resulting inefficiencies and increased cost, in both goods and people movement, would begin to erode private sector productivity gains and dampen the nation's economic recovery.

FINANCING ALTERNATIVES

There are only three possible sources of money to meet these vital needs:

1) GENERAL REVENUES: The pressures on the Federal budget to fund proven highway and transit requirements will continue and increase, and it is utterly unrealistic to expect such money to be provided from general funds.

2) STATE GASOLINE TAXES: Last year alone, more than forty states attempted to raise their gasoline tax to meet their <u>own</u> highway needs, and in more than 50% of the legislatures, these measures were rejected. If states are given even <u>greater</u> program responsibilities, they will simply <u>not</u> be able to raise the necessary funds.

3) INCREASED FEDERAL HIGHWAY USER CHARGES: An increase in the Federal highway user charge, as described in this proposal, offers the most dependable and realistic source of additional money to meet this national problem.

CONCLUSION

The serious deterioration of the nation's highway and mass transit capital infrastructure must be addressed at every level of government. Interest groups representing highway and transit users, as well as Congress, the States and the national media have recognized that regardless of who is ultimately responsible for the various programs, increased funds are necessary to simply maintain current performance levels on our highway and transit networks.

This highway user charge proposal will greatly benefit the Federalism initiative by reassuring state and local officials that those transportation programs selected for transfer are accompanied by sufficient revenues. Moreover, this initiative will bolster the Administration's user charge principle of one hundred percent recovery of allocable costs in all transportation modes. It will also provide a user based means to fund a critical national need, one that would otherwise result in additional demands on general Federal budget resources.

The Department of Transportation recommends an increase in annual highway user charges sufficient to raise $5 billion to bring current user fees into line with necessary expenditures. Of that amount $1 billion should be dedicated to capital assistance for mass transit.

____
RECOMMEND

____
NOT RECOMMEND

TABLE 1

Federal Cost Recovery

(Dollars in Millions)

Program	Current Federal Cost Recovery FY 1982		Proposed Cost Recovery	
	Dollars	Percent	Dollars	Percent
Deep Draft Ports[1]	$ 0	0%	$323	100%
Inland Waters (shallow draft nav.)	26	10	280	100
Coast Guard[2]	0	0	475-600	100
Aviation[3]	1305	50	2600	100
Highways[4]	7800	100	not avail.	100

1. Additional spending may be financed directly by state and local authorities.

2. Excludes defense, law enforcement and search and rescue in life-endangering situations.

3. Federal cost recovery for FAA programs was about 50% in FY 81. Because of the expiration of statutory authority, no revenues are currently being deposited into the Airport and Airway Trust Fund. In March 1981, the Administration proposed legislation that would reauthorize revenue deposits into the Aviation Trust Fund, change some of the user fees and finance 85% of FAA programs from the Trust Fund. This percentage represents 100% of FAA capital, operating and maintenance and other costs clearly allocable to System users. The New Federalism proposal would return some of these user charges to state and local government for local airport development.

4. The estimated receipts total $7.8 billion in FY 1982. Outlays are estimated at $8.3 billion. Actual cost recovery remains at 100 percent because there currently is a balance in the Highway Trust Fund that is being used to cover cash outlays.

TABLE 2

BUDGET EFFECTS OF INCREASED USER CHARGES

The following table summarizes the budget impacts of the DOT proposed increases in user charges compared to current user charges and program levels. These figures represent a conservative statement of the budget benefits, reflecting only the differences between user charge receipts and outlays, as computed in the Federal budget.

	FY83	FY84	FY85	FY86	FY83-86
User Charge Increase	5.5	5.4	5.3	5.2	21.4
Outlay Increase	.8	2.8	3.7	4.3	11.6
Budget Deficit Reductions	+4.7	+2.6	+1.6	+0.9	+9.8
HTF Balance*	12.7	14.7	15.2	14.8	---
Interest Increase	.2	.5	.7	.8	2.2

In addition to receipt/outlay differences, which determine the budget balance, an important secondary budget consideration is the amount of cash available in the Highway Trust Fund (HTF), which reduces federal borrowing needs in the private money market. HTF interest payments represent intergovernmental transfers not net outlays, thereby providing an important cash flow advantage to the government. Because the HTF balance is raised under the DOT proposal, $2.2B is generated in additional interest over the FY 1983-1986 period. Although such interest transactions are not visible in the federal budget, DOT believes that the imputed value of HTF interest payments must also be considered.

The total budget deficit reduction for FY 1983-86 is nearly $10 billion.

*These figures assume that all revenues would flow into the Highway Trust Fund. The accounting mechanics of the Federalsim Trust Fund are not yet resolved.

CM# 205

THE SECRETARY OF TRANSPORTATION

WASHINGTON, D.C. 20590

February 17, 1982

18 FEB 1982

MEMORANDUM TO THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM : Secretary Lewis Drew Lewis

Re : Near Term Future for U.S. Active Shipbuilding Base

There are 26 shipyards in the Active Shipbuilding Base. As a whole, the group faces a near-term decline in business activity and several individual shipyards are in serious trouble and may soon go out of business. From September 1979 through September 1981, total aggregate employment in the 26 shipyards remained relatively stable with some shipyards having employment increases while others have had employment decreases. This means that, as a composite, these shipyards have historically acquired a mix of new construction work, ship repair work,industrial work, and engineering work to support a relatively stable aggregate level of total employment.

Based upon completion of a recent industry assessment, aggregate direct labor for the 26 shipyards will likely decrease by about 28 percent during the next 15 month period unless new orders are received. In the absence of additional new construction contracts or a significant increase in ship repair contracts, the following 11 shipyards of the Active Shipbuilding Base will likely experience a serious reduction in direct labor requirements over the next 15 months.

Avondale Shipyards, Inc. (Avondale, Louisiana)
Bay Shipbuilding Corporation (Sturgeon Bay, Wisconsin)
Bethlehem Steel Corporation (Sparrows Point, Maryland)
General Dynamics Corporation (Quincy, Massachusetts)
Halter Marine, Inc. (New Orleans, Louisiana)
Levingston Shipbuilding Company (Orange, Texas)
National Steel & Shipbuilding Company (San Diego, California)
Peterson Builders, Inc. (Sturgeon Bay, Wisconsin)
Sun Ship, Inc. (Chester, Pennsylvania)
Todd Shipyards Corporation (Galveston, Texas)
Todd Shipyards Corporation (Houston, Texas)

Because of their traditional reliance on large commercial vessel construction projects, their small base of ship repair activity, and the present rapidly declining workload Avondale, Bay, Bethlehem (Sparrows Point), and General Dynamics (Quincy) are an immediate concern. Within the past two months, information has become available that Avondale could have sizable layoffs in 1982, Bethlehem (Sparrows Point) will run out of work before the end of 1982, and National Steel faces the prospect of laying off half of its work force in 1983. Work force reductions are projected exceeding 50 percent for each of these shipyards in 1982 except National Steel which will experience similar rapidly declin requirements by early 1983. The decline in shipyard activity has b further accelerated by the elimination of construction differential subsidy (CDS) funds for FY 1982 and amendments to the Merchant Marine Act of 1936, permitting foreign construction. Hence it is unlikely that U.S. shipyards will be awarded contracts in the near future for oceangoing ships engaged in the foreign trade. The FY 1982 reduction of the Maritime Administration's Federal Ship Financing Program (Title XI) to $675 million and loss of eligibility for drilling units has also resulted in another adverse impact on the U.S. shipyard employment.

Impact of Navy Shipbuilding Program

There is no doubt that U.S. Navy contract awards will dominate future shipbuilding activity in the 26 shipyards of the Active Shipbuilding Base. After analyzing the overall impact of out-year shipbuilding program, it is evident that projected Navy new construction contracts will not provide near-term work required for maintaining existing industry capacity and capability on a national basis. Furthermore, the Navy program will not provide an adequate workload in the long term for maintaining available facilities and work force, and a number of specific shipyards will not receive significant relief. One cannot predict with certainty which of the 11 threatened shipyards may go out of business because such actions involve private sector decisions taking into consideration a variety of business factors.

Conclusions

- Without immediate construction contracts, direct labor for the 26 shipyards in the Active Shipbuilding Base will decrease in the aggregate by approximately 28 percent during the next 15 month period.

- Eleven (11) shipyards are in serious trouble because of lack of work and are potential candidates to go out of business during the coming months. Any shipyard closure will result in the loss of skilled workers needed for out-year shipbuilding programs.

- The projected Navy shipbuilding program will not provide near term work for maintaining existing industry capacity nor will it sustain the complete Active Shipbuilding Base in the long term with respect to maintaining available facilities and work force.

The Department of Transportation, which is currently developing its maritime promotional program, will continue to monitor the status of the shipbuilding industry for the Cabinet Council on Economic Affairs.